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2 Honorable Samuel J. Steiner
September 3, 2004 9:30 a.m
3 **RESPONSE: AUGUST 30, 2004**
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5 UNITED STATES BANKRUPTCY COURT
6 WESTERN DISTRICT OF WASHINGTON AT SEATTLE

7 In re:
8 DANA QSR, INC.,
9 Debtor.
10
11

CASE NO. 04-18070 SJS
Chapter 11

**MEMORANDUM OF LAW IN
SUPPORT OF JOINT MOTION
FOR SUBSTANTIVE
CONSOLIDATION**

12 I. NATURE OF MOTION.

13 Dana QSR, Inc., (also referred to as "Dana") and Joly,
14 Inc., (also referred to as "Joly") seek entry of an order
15 substantively consolidating their separate chapter 11 cases. If
16 the motion is granted, the two companies will be administered as
17 one and all assets will be pooled for distribution to all
18 creditors pursuant to the requirements of the Bankruptcy Code.
19 Inter-company claims will be extinguished. And creditors of the
20 consolidated companies will be combined for the purpose of
21 voting on the reorganization plan.

22 This motion is supported by the declaration of David
23 Lively, President of each company, the attachments to his
24 declaration, and this Memorandum of Law.
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1 II. LAW.

2 2.1 Legal Basis for Substantive Consolidation.

3 There is no statute that specifically deals with
4 substantive consolidation. But the power to substantively
5 consolidate has been considered part of the court's general
6 equitable powers since passage of the Bankruptcy Act of 1898.
7 See In re Bonham, 229 F.3d 750 at 763 (9th Cir. 2000). The
8 power of substantive consolidation, though not codified by
9 either of the Bankruptcy Reform Acts of 1978 and 1994, derives
10 from the court's general equity powers as expressed by 11 U.S.C.
11 §105(a), which states:

12 The court may issue any order, process, or
13 judgment that is necessary or appropriate to
14 carry out the provisions of this title ...

15 Various courts have developed different tests for
16 determining if substantive consolidation is appropriate. These
17 courts have had to deal with substantive consolidation on a case
18 by case basis.

19 The Ninth Circuit has adopted the test used by the
20 Second Circuit in the case of In re Augie/Restivo, 860 F.2d 515,
21 at 518 (2nd Cir. 1988). In Augie the court applied a test which
22 considered two factors: "(1) whether creditors dealt with the
23 entities as a single economic unit and did not rely on their
24 separate identity in extending credit; or (2) whether the
25 affairs of the Debtor are so entangled that consolidation will
26 benefit all creditors." Augie/Restivo, 860 F.2d at 518. The
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1 presence of either factor is a sufficient basis to order
2 substantive consolidation.

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4 **III. THE AFFAIRS OF JOLY AND DANA ARE SO ENTANGLED THAT**
5 **CONSOLIDATION WILL BENEFIT ALL CREDITORS.**

6 Dana and Joly have the same shareholders. They are both
7 managed by Dave Lively. They are both in the same business.
8 Joly owns and manages three Burger King franchises. Dana owns
9 and manages two Burger King franchises. All of these franchises
10 are in the greater Seattle area.

11 The vendors are the same. Neither company has a line of
12 credit with a commercial bank. Each company lives off its cash
13 flow. As stated by Mr. Lively in his declaration, each company
14 would, from time to time, pay debts of the other company.

15 Originally there were good reasons to keep the two
16 companies separate. Joly was formed to buy out a partner of
17 Nancy Jones and Dave Lively and insulate the new company from
18 the debts of the former partner. Dana was formed to acquire two
19 Burger King franchises and provide even more insulation from the
20 financial difficulties of the former partner. Now that reason
21 no longer exists. And Mr. Lively has tended to operate the two
22 businesses as one entity.

23 Consolidation will benefit the debtors and all creditors
24 because all administrative expenses will be substantially
25 reduced making a distribution to creditors far more likely. The
26 reduction of administrative expenses was a significant factor in
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1 the case of In re Standard Brands Paint Company, 154 BR 563, 571
2 Bankr. CD Cal. 1993. Substantive consolidation was granted in
3 that case. If the cases are consolidated, Shafer & Bailey,
4 counsel for Joly, will no longer have a conflict. It will be
5 able to represent both companies. This will reduce the
6 attorneys fees that accrue in bankruptcy. Likewise, one
7 accountant would be able to perform services for the
8 consolidated entity also reducing fees. Since fees of
9 professionals are administrative claims and must be paid in full
10 on confirmation, these fees will be reduced making confirmation
11 more likely.

12 Also, consolidation of the two cases would eliminate the
13 possibility that each Debtor would accrue additional fees in
14 analyzing the claims each may have against the other. Such
15 claims usually have more of a hypothetical than a real value.
16 But sometimes, because of pressure from creditors or from the US
17 Trustee, debtors are forced to analyze and even pursue such
18 claims where the net result will be to diminish the bankruptcy
19 estate by increasing administrative expenses.

20
21 **CONCLUSION.**

22 If these cases are substantively consolidated,
23 administrative expenses, which sometimes swallow cases, will be
24 significantly reduced. Further the companies can spend minimal
25 time analyzing inter-corporate transfers as these transfers
26 become extinguished upon substantive consolidation. The

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1 consolidated Debtor can focus its efforts on more productive
2 activities.

3 Respectfully submitted this 12th day of August, 2004.

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5 SHAFER & BAILEY

6
7 /s/ James W. Shafer
8 James W. Shafer WSBA# 8011
9 Attorney for Debtor
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Dana consolidation mem.wpd

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